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Brief on Tax Laws (Amendment) Ordinance, 2020

(for Builders, Developers and Construction Industry)

Preamble

The Tax Laws (Amendment) Ordinance, 2020 [the Amendment Ordinance] follows through on the Special Incentive Package announced by the Prime Minister in early April for revival of construction sector in backdrop of deterioration of macroeconomic indicators. To promote and support the sector, Prime Minister had announced grant of industry status to the sector along with formation of Construction Industry Development Board. The construction industry and many allied sectors have also been exempted from lockdowns otherwise in force in the country to arrest Covid-19 pandemic. It is expected that the amendments made through the Amendment Ordinance will be incorporated through the upcoming Finance Bill, 2020.

To align with this announcement, the Amendment Ordinance grants status of 'industry' to construction sector through suitable amendment in the Income Tax Ordinance, 2001 [the 2001 Ordinance] and offers several time bound tax reliefs to builders and developers who complete their projects by September 2022. Many of these concessions are optional. Those who decide not to opt for the tax rates offered by the newly promulgated Eleventh Schedule may continue to be taxed under normal tax regime. The Amendment Ordinance also grants immunity from probe regarding source of investment, subject to fulfillment of certain conditions, though it is noted that immunity is restricted to the provisions of the 2001 Ordinance and does not cover the Banami Transactions (Prohibition) Act, 2017. The Amendment Ordinance is also silent on any exemptions from sales tax or excise duty on construction material, though this was also part of the package announced by the Prime Minister. There is also no relief from capital gains tax on commercial property or open plots despite announcement to the contrary.

It however needs to be seen as to how grant of a blanket immunity from questioning the source of investment is taken by Financial Action Task Force [FATF] as action against illegal money, money value transfer services (such as Hundi-hawala) is one of the outstanding conditions of FATF to get the country out of FATF grey list.

This publication contains an overview of the salient features of the amendments. We recommend that while considering the application of the amendments to any case, reference be made to the specific wordings of the relevant statutes.

This brief can also be accessed on our website www.kpmg.com.pk

19 April 2020

Tax Laws (Amendment) Ordinance, 2020

Scope of industrial undertaking enhanced

The Amendment Ordinance enhances the scope of 'industrial undertaking' as the said term stands defined in the 2001 Ordinance so as to include the following with effect from 01 May 2020:

a person directly involved in the construction of buildings, roads, bridges and other such structures or the development of land, to the extent and for the purpose of import of plant and machinery to be utilized in such activity, subject to such conditions as may be notified by the Board.

With this amendment, the construction sector is now entitled to seek exemption from advance tax otherwise collectible on import of plant and machinery, besides claim of tax credit under section 65D of the 2001 Ordinance on income from new projects insofar the special tax regime under the newly promulgated Eleventh Schedule is not opted for. The said credit is however not available to non-corporate sector.

Special tax regime for Builders and Developers

The Amendment Ordinance lays down special provisions for taxation of builders and developers on a project specific basis. For this purpose, 'builder' and 'developer' has been defined. This also provides for protection from probe into their sources. These are discussed hereunder:

Taxation of Builders and Developers

From tax year 2020 and onwards, a builder or a developer can opt for paying tax under a special tax regime. For those who opt for this scheme, tax shall be computed in accordance with the rules and rates provided under the Eleventh Schedule on a project to project basis for:

a) a new project to be completed by 30

September 2022; and

b) an incomplete existing project to be completed by 30 September 2022.

This is however subject to the following conditions:

- Income under the Eleventh Schedule shall not be chargeable to tax under any head of income in computing taxable income of the person;
- No deduction shall be allowable under the 2001 Ordinance for any expenditure incurred in deriving the income;
- The mount of the income shall not be reduced by:
 - any deductible allowance i.e. Zakat, WPPF, WWF etc. and
 - set-off of any loss;
- No credit shall be allowed against tax computed under the Eleventh Schedule except advance tax collected after 17 April 2020 under section 236K of the 2001 Ordinance on purchase of an immoveable property utilized in an eligible project;
- there shall be no refund of any tax collected or deducted under the 2001 Ordinance;

Section 113 and 113C of the 2001 Ordinance (regarding minimum tax and alternate corporate tax) will not apply on income, profits and gains of a builder or developer from eligible projects.

Any income of a builder and developer other than income, profits and gains subject to this regime shall continue to be subject to taxation as per the provisions of 2001 Ordinance.

Qualified Builders and Developers

"Builder" and "Developer" registered on project to project basis on FBR website and means a single object company, or a single object limited

liability partnership registered with the SECP, or an association of persons registered under the Partnership Act, 1932 as set up during the period starting 17 April 2020 to 31 December 2020.

The sole object of “builder” is construction of buildings and their disposal.

The sole object of “developer” is development of land of any kind either for itself or otherwise.

Qualified Projects

Qualified projects in case of “builder” and “developer” are those which are:

- set up between 17 April 2020 and 31 December 2020 and completed by 30 September 2022 (i.e. new projects)
- set up prior to 17 April 2020 and completed by 30 September 2022 (i.e. existing projects).

Estimated life span of a project shall not exceed two and a half (2.5) years.

A project shall be considered commenced:

- In case of a construction project, on the date when the layout plan is approved by the concerned authority; and
- In case of developers, the date when the development plan is approved by the concerned authority.

In case the builder or developer has taken all necessary steps to procure all approvals, but such approval is delayed for more than 30 days, and resultantly the cut-off date of 31 December is not met, FBR has been empowered to provisionally accept commencement of such projects on a case to case basis.

A project shall stand completed:

- For a builder, the date on which:
 - the grey structure is completed – that is when the roof of the top floor has been laid as per the approved plan.

- For a developer, the date on which:
 - at least 50% of the total plots have been booked in the name of buyers; and
 - at least 40% of the sale proceeds have been received;
 - landscaping has been completed; and
 - at least 50% of the roads have been laid up to subgrade level as certified by the approving authority or NESPAK.

Immunity from probe

The Amendment Ordinance provides protection from probe viz-a-viz nature and sources of investment made with respect to:

- any amount invested as capital in a building, or
- any amount invested as capital in a land possessed or acquired by the builder or developer, or its partner in case of a limited liability partnership or in association of persons if the amount is
 - invested as capital or the land is transferred on or before 31 December 2020 in the manner as prescribed; and
 - is utilized in a construction or development project under sub section (2) in the manner as prescribed:
 - the first purchaser of newly constructed buildings of a project under sub-section (2) if the purchase is made on or before the 30 September 2022 in the manner as prescribed.

The immunity is however subject to following conditions:

- Individual builders and developers who intend to make investment in the form of money or land in a new project shall be required to

- open a new bank account and transfer / deposit money into it on or before 31 December 2020 where investment is in the form of money;
- have the ownership title of land at 17 April 2020 where investment is in the form of land.
- In case of a company or AOP who intends to make investment in the form of money or land in a new project:
 - that it should be a single object (builder or developer) company or AOP formed after 17 April 2020 and before 31 December 2020;
 - the person shall be a member or shareholder of such association of persons or company, as the case may be;
 - if capital investment is in the form of money, such amount shall be invested through crossed banking instrument only on or before 31 December 2020; or
 - if capital investment is made in the form of land, such land shall be transferred to the builder or developer on or before 31 December 2020.

Capital investment means investment as equity resources and does not include borrowed funds.

Provided that the person has the ownership title of land at 7 April 2020:

- in respect of purchase price paid by the first purchaser of a building to builder
- In case of purchase from a new project or from an existing incomplete project
- full or balance payment, as the case maybe, is made through a crossed banking instrument between the date of registration of the project with the Board and 30 September 2022

The term “first purchaser” means a person who purchases a building or a unit directly from the builder and does not include a subsequent or a substituted buyer.

- In case of a purchaser of plot who intends to construct a building thereon, if
 - the purchase is made on or before 31 December 2020;
 - full payment is made on or before 31 December 2020 through a crossed banking instrument;
 - construction on such plot is commenced on or before 31 December 2020;
 - construction is completed by 30 September 2022; and
 - the person registers himself with the Board on the online IRIS portal.

The protection from probe into nature and sources of fund shall be available if following conditions are met:

- The purchase price of a plot shall be the higher of:
 - 130% of the fair market value as determined by the Board under section 68(4) of the 2001 Ordinance; or
 - at the option of the purchaser, the lower of the values determined by at least two independent valuers from the list of valuers approved by the State Bank of Pakistan.
- The money or land invested shall be wholly utilized in the project.
- A person making an investment shall submit a prescribed form on IRIS web portal.
- Map approving authorities or NESPAK in case of builder shall certify that grey structure as per approved map has been completed by the builder by 30 September

2022.

- Map approving authority or NESPAK in case of developer shall certify that;
- landscaping has been done by 30 September 2022, and
- at least 50% of the roads have been laid up to sub-grade level.
- An ICAP QCR rated firm of chartered accountants notified by the Board shall certify that 50% plots have been booked for sale and at least 40% proceeds have been received by 30 September 2022.

Persons who can be probed

The protection from probe under the 2001 Ordinance 2001 shall not apply to the following persons

- holder of any public office as defined in the Voluntary Declaration of Domestic Asset Act 2018 or
- his benamidar as defined in the Benami Transactions (Prohibition) Act, 2017 (V of 2017) or his spouse or dependents;
- a public company, a real estate investment trust and a company whose income is exempt under any provision of the 2001 Ordinance; or
- any proceeds derived from the commission of a criminal offence including crime of money laundering, extortion or terror financing, excluding offences under tax laws.

Change in pattern of ownership of a builder or developer before completion of a project

- A shareholder or a partner in a builder or developer shall not be allowed a change in ownership of an incomplete project without prior approval of FBR. However, in case of

hardship, the Board may allow such change in ownership subject to conditions and restrictions as it may deem fit on a case to case basis.

- FBR may allow succession to legal heirs in case of deceased shareholder or a partner as well as allowing additional partners or shareholders after 31 December 2020. However, the additional partners or shareholders shall not be eligible for immunity from probe with respect to their source of investment.

Incorporation of profits and gains

A builder or developer opting for taxation under the special regime shall not be allowed to incorporate profits and gains accruing from such projects in excess of ten times of the tax paid under eleventh schedule.

Investments made pursuant to the Amendment Ordinance could be admissible in evidence against the persons

Any Investments made pursuant to this Ordinance could be admissible in evidence against the person for the purposes of any proceedings relating to imposition of penalty or adverse action for the purposes of prosecution under any law except the 2001 Ordinance.

Dividend income exempted

Dividend income received by a person from the builder or developer being a company out of the profits and gains derived from a project shall be exempt from tax.

Exemption from capital gain tax

Capital gains derived by a resident individual from the sale of constructed residential property has been declared exempt subject to the following conditions:

- the residential property was being used for personal accommodation by the resident individual, his spouse or dependents and for which any of the utility bills have been issued in the name of such individual;
- the land area of the property does not exceed 500 square yards in case of a house and 4,000 square feet in case of a flat; and
- exemption under this clause has not previously been availed by the individual, his spouse or dependents.

Exemption from withholding of tax

Builders and developers are no more required to withhold tax under section 153 of the 2001 Ordinance on:

- purchase of building material except steel and cement.
- on services of plumbing, electrification, shuttering and other similar and allied services obtained from non-corporate service providers.

Builders and developers being a company are no more obliged to withhold tax under section 150 of the Ordinance, 2001 on dividend payment to a person from profits and gains from a new project.

Cessation of capital valuation tax

Collection of Capital Value Tax stands ceased effective 17 April 2020 with respect to assets or a right to use for 20 years acquired thereafter.

Computation of tax liability

Profit and gains and tax payable thereon shall be computed under Eleventh schedule in the following manner

- (a) The tax liability shall be computed for the project on annual basis. The annual tax liability shall be worked out as under:

Tax Liability as per rates (Annexure)

Estimated project life

- (b) The estimated project life shall be treated as three years from tax year 2020 through tax year 2022, and the tax payable shall be reduced by the percentage of completion up to the last day of the accounting period pertaining to tax year 2019.

The tax liability so calculated and paid shall be final tax.

The tax so computed shall be paid in advance in 4 equal quarterly installments under section 147 of 2001 Ordinance.

In case of development of plots and construction of buildings on the same plots, both rates shall apply.

For low-cost projects developed or approved by Naya Pakistan Housing and Development Authority (NAPHDA) or under the Ehsaas programme, the tax rates levied will be reduced by 90%.

In case of development of plots and construction of buildings on the same plots for low cost housing and all projects developed by NAPHDA, the higher rates shall apply.

Registration and filing requirements

- All persons registered under this scheme shall submit the registration form along with the irrevocable option to be assessed under the Eleventh Schedule in respect of each project on IRIS through FBR website by 31 December 2020 or within 30 days of setting up of project, whichever is earlier.
- A builder or developer availing this scheme shall electronically file a return of income and wealth statement as may be prescribed, accompanied with evidence of payment of due tax which shall be taken for all purposes of the Ordinance to be an assessment order issued to the taxpayer by the Commissioner

to the extent of income computed under the special rules.

- Return and Wealth Statement filed can be revised within 60 days of the date of filing without approval of the Commissioner.

Certification

Every builder or developer shall be required to obtain a certificate in the prescribed manner from approving authority or map approving authority or NESPAK, as the case maybe, to the following effect:

- Total land area, covered area and saleable area of the project in square foot or square yard
- Such other documents as may be prescribed by the Board.

Every builder or developer shall be required to provide such certificate to FBR

Rate of advance tax in case of sale by auction

In case of immovable property sold by auction, the rate of collection of tax shall be 5% of the gross sale price.

Rate of Tax

Annexure

Persons	Property Type	Area	(A) Karachi, Lahore and Islamabad	(B) Hyderabad, Sukkur, Multan, Faisalabad, Rawalpindi, Gujranwala, Sahiwal, Peshawar, Mardan, Abbottabad, Quetta	Urban Areas not specified in A and B
		Area in Sq. Ft.	Rate per Sq. ft.		
Tax on Builders	Commercial Buildings	Any size	Rs.250	Rs.230	Rs.210
	Residential Building	up to 3000	Rs.80	Rs.65	Rs.50
		Morthan 3000 & above	Rs.125	Rs.110	Rs.100
		Area in Sq. yd.	Rate per Sq. yd		
Tax on Developers	Entire Project (Other than Industrial Area)	Any size	Rs. 150	Rs. 130	Rs. 100
	Development of Industrial Area	Any size	Rs.20	Rs.20	Rs.10



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